

## Message Text

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ORIGIN EB-11

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AF/EPS: MR. KENNEY (INFO)

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FM SECSTATE WASHDC

TO USINT CAIRO

USINT ALGIERS

AMEMBASSY AMMAN

AMEMBASSY BEIRUT

AMEMBASSY JIDDA

AMEMBASSY KHARTOUM

AMEMBASSY KUWAIT

AMEMBASSY RABAT

AMEMBASSY TUNIS

AMEMBASSY TRIPOLI

AMEMBASSY ABU DHABI

AMEMBASSY TEHRAN

C O N F I D E N T I A L STATE 157536

E.O. 11632: N/A

TAGS: OVIP

SUBJECT: ARAB LEAGUE CALLS MEETING TO DISCUSS ARAB RESERVES

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REF: A. CAIRO 2344; B. STATE 138408

1. TEXT OF U.S. PAPER ON SUBJECT CIRCULATED TO C-20

DEPUTIES JULY 17, 1973 IS REPRODUCED BELOW. YOU SHOULD AS-

SURE YOURSELF THAT APPROPRIATE OFFICIALS OF HOST GOVERNMENTS HAVE FULL AND CORRECT TEXT OF U.S. PAPER, AND, IF APPROPRIATE AS SUGGESTED IN REF A., POINT OUT THAT THE PAPER MAKES CLEAR IN ITS FIRST NUMBERED PARAGRAPH THAT NOTHING IN THE U.S. POSITION PRECLUDES OR IS INTENDED TO PRECLUDE INVESTMENTS IN ARAB WORLD OR ANYWHERE ELSE.

2. YOU WILL NOTE THAT THERE REMAIN SOME IMPORTANT POINTS REQUIRING MORE PRECISE DEFINITION, ESPECIALLY IN PARAGRAPH 3 NUMBERED OF C-20 DOCUMENT. THESE POINTS WILL BE DISCUSSED IN APPROPRIATE TECHNICAL FORUMS. WE DONOT CONSIDER IT ADVISABLE TO ATTEMPT FURTHER INTERPRETATIVES THROUGH DIPLOMATIC CHANNELS AT THIS TIME.

3. FYI. ONLY MAJOR OBJECTIVE OF INVESTMENT FUNDS IS NOT TO

PRECLUDE "SPECULATIVE ACTIVITY", AS IMPLIED REF TEL A. TO GIVE ARAB STATES THIS IMPRESSION MIGHT BE MIS-INTERPRETED AS CONTRADICTING FREE MOBILITY OFFERED IN NUMBERED PARAGRAPHS 1 AND 2 OF C-20 DOCUMENT. END FYI

4. TEXT FOLLOWS, "INVESTMENT IN OWNERSHIP OF ASSETS IN ONE COUNTRY BY PRIVATE NATIONALS OF ANOTHER HAS AT TIMES GIVEN RISE TO ECONOMIC OR POLITICAL PROBLEMS THAT HAVE REQUIRED RESOLUTION. HITHERTO, SUCH FOREIGN OWNERSHIP HAS NOT BEEN DIRECTLY BY GOVERNMENTS ON A LARGE SCALE, EXCEPT IN THE FORM OF ASSETS HELD AS MONETARY RESERVES. IN FUTURE, HOWEVER, THE GOVERNMENT OWNERSHIP OF LARGE FOREIGN INVESTMENTS ON THE PART OF A FEW OIL-PRODUCING COUNTRIES IS LIKELY TO BE DESIRABLE, AND MAY WELL SURPASS IN SIZE ANY COMPARABLE SITUATION IN THE PAST. THE DEGREE OF STABILITY OF SUCH HOLDINGS OF FOREIGN ASSETS COULD THEORETICALLY PLAY A POSITIVE OR NEGATIVE ROLE IN THE EFFECTIVENESS OF ANY INTERNATIONAL MONETARY SYSTEM, AND THEREFORE HAS BEEN MENTIONED AS A MATTER OF CONCERN, WHETHER OR NOT SUCH HOLDINGS ARE TECHNICALLY CONSIDERED AS PART OF THE "RESERVES" OF THE INVESTING COUNTRY OR WERE OUTSIDE SUCH "RESERVES." IN JUDGING THE DESIGN OF ANY NEW INTERNATIONAL MONETARY SYSTEM, THE QUESTION WILL BE ASKED AS TO THE MEANS, IF ANY, PROVIDED  
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FOR HANDLING THIS SITUATION. IN APPROACHING THIS QUESTION, WE HAVE FELT IT ESSENTIAL THAT THE INTERESTS OF THE INVESTING COUNTRIES THEMSELVES IN FREEDOM FOR THEIR INVESTMENT POLICIES BE FULLY RECOGNIZED.

IN THE FRAMEWORK OF THE U.S. PROPOSALS FOR THE ADJUSTMENT PROCESS, MOVEMENTS IN TOTAL RESERVES OF A COUNTRY WOULD ASSUME A PREDOMINANT ROLE AS AN "OBJECTIVE INDICATOR," OF THE NEED TO TAKE ADJUSTMENT ACTION AND RESERVES WOULD IN GENERAL NEED TO BE BROADLY DEFINED FOR THIS PURPOSE TO INCLUDE A WIDE RANGE OF FOREIGN ASSETS HELD BY NATIONAL GOVERNMENTAL AUTHORITIES. HOWEVER, IT IS ALSO FULLY RECOGNIZED THAT IN CERTAIN UNUSUAL CIRCUMSTANCES IN A LIMITED

NUMBER OF COUNTRIES, IT MAY BE BOTH UNNECESSARY AND UNDERSIRABLE TO RETAIN SO BROAD A DEFINITION OF RESERVES, OR FOR THE SYSTEM TO REQUIRE BALANCE OF PAYMENTS "ADJUSTMENT" ACTION WHEN "RESERVES" REMAIN ABOVE CERTAIN PREDETERMINED POINTS. THIS WOULD BE PARTICULARLY THE CASE IN THE CIRCUMSTANCES OF CERTAIN OIL-EXPORTING COUNTRIES WHICH EXHIBIT A PERSISTENT STRUCTURAL TENDENCY TO ACQUIRE FOREIGN ASSETS ESSENTIALLY IN EXCHANGE FOR ASSETS "FROM THE GROUND."

AS SECRETARY SHULTZ OBSERVED IN AN ADDRESS DELIVERED IN PARIS JUNE 6, 1973:

- -  
CERTAINLY, AS WE POINTED OUT IN PRESENTING OUR MONETARY PLANS, THE ACCUMULATION OF LARGE CURRENT SURPLUSES BY ARABIAN PENINSULAR STATES SHOULD NOT CALL FOR EXCHANGE RATE ADJUSTMENT ACTIONS ON THEIR PART. WHILE MANY OF THEIR

EXTERNAL INVESTMENTS MIGHT LOOSELY BE CONSIDERED RESERVES, CERTAINLY THEY ARE NOT COMPARABLE TO THE KIND OF MONETARY RESERVES THAT WOULD SUGGEST A NEED FOR MONETARY ADJUSTMENT ACTION ON THEIR PART.

INSOFAR AS FOREIGN EARNINGS ARE SPENT FOR IMPORTS OF GOODS AND SERVICES NECESSARY TO SECURE DOMESTIC DEVELOPMENT AND DIVERSIFICATION OF A COUNTRY'S ECONOMIC RESOURCES, SO THAT THE COUNTRY'S INTERNATIONAL RESERVES DO NOT POINT TO ADJUSTMENT ACTION, THE PROPOSED SYSTEM WOULD BE SATISFACTORY.

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FIED. INDEED, PROMOTION OF DOMESTIC ECONOMIC DEVELOPMENT IS CLEARLY A HIGHLY SATISFACTORY MEANS OF UTILIZING POTENTIAL SURPLUSES FROM THE INTERNATIONAL AS WELL AS DOMESTIC POINT OF VIEW. THIS WOULD, OF COURSE, BE THE CASE WITHOUT REGARD TO WHETHER THE SOURCE OF THE POTENTIAL SURPLUS WERE TO ARISE FROM OIL PRODUCTION OR OTHERWISE. ECONOMIC ASSISTANCE TO OTHER COUNTRIES, INCLUDING TO COUNTRIES IN THE SAME GEOGRAPHIC REGION, WOULD ALSO OBVIOUSLY BE A SATISFACTORY WAY OF AVOIDING OR DISPOSING OF POTENTIAL SURPLUSES. IN THESE INSTANCES, THE SYSTEM PROPOSED BY THE UNITED STATES WOULD APPLY EQUALLY TO ALL COUNTRIES AND THE GREAT MAJORITY OF ALL COUNTRIES WHEN TENDING TOWARD SURPLUS (INCLUDING OIL-PRODUCING COUNTRIES WITH LARGE POPULATIONS AND LARGE FINANCIAL REQUIREMENTS FOR DEVELOPMENT) WOULD BE COVERED BY WHAT HAS BEEN SAID ABOVE.

THE ONLY PRACTICAL PROBLEM IN TERMS OF THE PROPOSED SYSTEM, ARISES WITH RESPECT TO A VERY FEW OIL-PRODUCING COUNTRIES WHERE THE POTENTIAL FOREIGN RECEIPTS COULD BE SUBSTANTIALLY LARGER THAN COULD PRACTICALLY AND PRODUCTIVELY BE SPENT FOR DOMESTIC DEVELOPMENT IN THE NEAR FUTURE. IT WOULD NOT BE IN THE GENERAL INTERNATIONAL INTEREST, OR IN THE INTEREST OF THOSE OIL-PRODUCING COUNTRIES, OR IN THE INTEREST OF THOSE POTENTIALLY RECEIVING INVESTMENT, FOR

THE OPERATION OF THE INTERNATIONAL MONETARY SYSTEM TO GIVE SUCH COUNTRIES ANY DISINCENTIVE TO THE PRODUCTION AND EXPORT OF OIL, OR FOR THEM TO UNDERTAKE ADJUSTMENT MEASURES (INCLUDING EXCHANGE RATE CHANGES) OUT OF KEEPING WITH THE DEVELOPMENT OF NON-OIL SECTORS OF THE ECONOMY. CLEARLY, APPROPRIATE AND MUTUALLY DESIRABLE ADJUSTMENT IN THESE INSTANCES CAN BE ACHIEVED BY CAPITAL EXPORTS, SO THAT POTENTIAL SURPLUSES OF SUCH OIL-PRODUCING COUNTRIES ARE AVOIDED BY FINDING INVESTMENT OUTLETS ABROAD ADVANTAGEOUS TO THE PRODUCERS THEMSELVES. THE ONLY COMPLICATING ELEMENT, IN TERMS OF THE U.S. PROPOSAL, IS THAT THESE CAPITAL EXPORTS MAY HAVE AN UNUSUAL CHARACTERISTIC, IN THAT THEY ARE OWNED AND MANAGED FOR THE MOST PART BY PUBLIC BODIES; FOR THAT

REASON THEY MAY FALL WITHIN THE RELATIVELY WIDE DEFINITION  
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OF "RESERVES" SUITABLE IN THE GENERAL OPERATION OF THE SYSTEM AS APPLIED TO ALL OTHER COUNTRIES.

OUR THINKING IS THAT THIS PROBLEM CAN BE RESOLVED IN A CONSTRUCTIVE AND MUTUALLY BENEFICIAL WAY BY PROVIDING IN THESE CIRCUMSTANCES FOR OFFICIAL INTERNATIONAL RECOGNITION THAT A PORTION OF THE FOREIGN ASSETS HELD BY SUCH A COUNTRY COULD APPROPRIATELY BE CONSIDERED NOT AS MONETARY RESERVE BUT RATHER AS A NATIONAL "INVESTMENT FUNDS" THIS FUND WOULD, AT THE DISCRETION OF THE PRODUCING COUNTRY, SIMPLY BE AN AGGREGATE ACCOUNTING OR DESIGNATION OF CERTAIN NATIONAL INVESTMENTS WHICH IT WANTS TO REMOVE FROM ITS "RESERVES," AND WHICH BY THE SAME TOKEN WOULD FALL OUTSIDE THE SYSTEM BY WHICH PRESUMPTION OF A NEED TO TAKE OTHER ADJUSTMENT ACTION WOULD ARISE. TO USE SECRETARY SHULTZ' WORDS AGAIN, IN HANDLING THESE INVESTMENT FUNDS THERE WOULD EXIST "ALL THE INGREDIENTS OF A HIGHLY ADVANTAGEOUS MUTUAL BARGAIN." THOSE OIL-EXPORTING COUNTRIES FOR WHICH IT WOULD BE DESIRABLE FROM EVERY VIEWPOINT TO INVEST SUBSTANTIAL FUNDS ABROAD WOULD WANT SECURITY AND A REASONABLE RETURN ON THEIR INVESTMENTS. MANY POTENTIAL RECIPIENTS OF THE INVESTMENT WOULD WELCOME IT IF THEY WERE SATISFIED IT WOULD BE REASONABLY STABLE AND BENEFICIAL.

WITHOUT ATTEMPTING TO SPELL OUT ARRANGEMENTS THAT MIGHT BE MADE IN MORE DETAIL THAN IS NECESSARY AT THIS STAGE, A FEW POINTS OF BROAD PRINCIPLE CAN BE MENTIONED WHICH WOULD SEEM TO US SUFFICIENT FOR THE PURPOSES OF THE PROPOSED SYSTEM:

1. INVESTING COUNTRIES ESTABLISHING AN "INVESTMENT FUND" MUST CLEARLY BE GUARANTEED THAT NOTHING IN THEIR DECISION TO DESIGNATE SUCH A FUND DETRACTS FROM THEIR INHERENT RIGHT TO MANAGE THEIR PORTFOLIOS OF INVESTMENT ABROAD SO AS TO SEEK TO

FULFILL THE INVESTMENT OBJECTIVES WHICH IN  
THEIR VIEW WILL BENEFIT THEIR ECONOMICS AND  
PEOPLES. TO PROTECT THIS RIGHT, WE DO NOT CON-  
TEMPLATE THAT THE IMF OR ANY OTHER OFFICIAL BODY  
WOULD HAVE ANY AUTHORITY TO MAKE PROPOSALS TO  
"INVESTMENT FUND" COUNTRIES WITH RESPECT TO THE  
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AMOUNT, NATURE OR LOCATION OF THEIR INVESTMENTS.

2. COUNTRIES POTENTIALLY ON THE RECEIVING SIDE OF  
INVESTMENT FROM OIL-PRODUCING COUNTRIES, OR FROM  
ANY COUNTRY, NOW HAVE THE INHERENT RIGHT TO PER-  
MIT THOSE INVESTMENTS, TO ENCOURAGE THEM, TO

LIMIT THEM, OR EVEN TO EXCLUDE THEM. THESE  
RIGHTS WOULD NOT BE BASICALLY ALTERED BY THE  
"INVESTMENT FUND" APPROACH. INDEED, MANY POTEN-  
TIAL INVESTMENT RECEIVING COUNTRIES WOULD BE  
LIKELY TO WELCOME THESE INVESTMENTS TO THE EX-  
TENT THEY FELT CONFIDENT THAT THEY WOULD BE  
LIKELY TO REMAIN OVER SUSTAINED PERIODS OF TIME,  
AND WOULD NOT BE SWITCHED SUDDENLY AMONG COUN-  
TRIES IN LARGE AMOUNTS WHICH COULD CONTRIBUTE TO  
DISRUPTIVE EXCHANGE MARKET CONDITIONS. AS A  
PRACTICAL MATTER, SINCE IN SOME CASES THE  
AMOUNTS OF "INVESTMENT FUND" INVESTMENT COULD  
REACH LARGE VOLUMES, THE INVESTING AND INVEST-  
MENT RECEIVING COUNTRIES MIGHT WISH IN SOME IN-  
STANCES TO ARRANGE SUCH BILATERAL CONTACTS,  
UNDERSTANDINGS OR AGREEMENTS AS THEY WOULD CON-  
SIDER MUTUALLY AGREEABLE, INCLUDING ASSURANCES  
THAT THE INVESTMENT RECEIVING COUNTRY WOULD NOT  
REDUCE THE AMOUNT OF "INVESTMENT FUND" INVEST-  
MENT ALREADY PLACED IN THAT COUNTRY WITHOUT FULL  
AGREEMENT OF THE AFFECTED "INVESTMENT FUND"  
COUNTRY.

3. THE INTERNATIONAL FINANCIAL COMMUNITY THROUGH  
THE IMF WOULD HAVE AN INTEREST ONLY IN SATISFING  
ITSELF THAT ARRANGEMENTS WITH RESPECT TO "INVEST-  
MENT FUNDS" ARE NOT INCONSISTENT WITH A SMOOTH  
AND EFFICIENT FUNCTIONING OF THE INTERNATIONAL  
MONETARY SYSTEM. TO AVOID ESTABLISHMENT OF  
"INVESTMENT FUNDS" BY COUNTRIES WHERE SUCH FUNDS  
WOULD BE INAPPROPRIATE, IMF APPROVAL MIGHT BE  
REQUIRED FOR THE ESTABLISHMENT OF ANY INDIVIDUAL  
COUNTRY'S "INVESTMENT FUND." SUCH APPROVAL

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SHOULD BE LIMITED TO THE CASES OF OIL-PRODUCING COUNTRIES WHOSE CIRCUMSTANCES EFFECTIVELY PRECLUDE ALL OF FOREIGN EARNINGS FROM BEING SOUNDLY SPENT FOR DOMESTIC DEVELOPMENT FOR THE FORESEEABLE FUTURE.

4. A STATISTICAL REPORTING SYSTEM COULD BE NEEDED TO ENABLE THE FUNCTIONS MENTIONED IN PARAGRAPHS 1., 2., AND 3., TO BE EXERCISED. "INVESTMENT FUND" COUNTRIES MIGHT BE REQUIRED TO PROVIDE TO THE IMF QUARTERLY STATISTICS COMPARABLE TO THOSE TO BE REQUIRED MONTHLY FOR ALL COUNTRIES IN REPORTING OFFICIAL FOREIGN EXCHANGE RESERVES IN

THE NEW MONETARY SYSTEM. AT THE PRESENT STAGE, THE U.S. VIEW IS THAT SUCH REPORTS ON OFFICIAL FOREIGN EXCHANGE HOLDINGS WOULD NEED TO INCLUDE: (A) THE AGGREGATE AMOUNT, (B) THE DISTRIBUTION OF THIS AGGREGATE AMOUNT FOREIGN COUNTRIES, AND (C) THE DISTRIBUTION OF THE AGGREGATE AMOUNT IN TERMS OF ITS VALUATION BY CURRENCIES OR OTHERWISE. THE INFORMATION WOULD BE MADE AVAILABLE TO ALL EXECUTIVE DIRECTORS, IF THE EXTENT OF GEOGRAPHIC AND CURRENCY DETAIL DOES NOT GO BEYOND WHAT IS REQUIRED IN REPORTING IN A REFORMED SYSTEM WITH RESPECT TO FOREIGN EXCHANGE HOLDINGS IN THE "RESERVES" OF ALL MEMBERS. IN RESPECT TO THE DATA FROM STATISTICAL REPORTING REQUIREMENTS, THE FUND'S POWERS WOULD BE LIMITED TO THE USE OF THOSE STATISTICS MADE AVAILABLE TO ALL EXECUTIVE DIRECTORS IN THE CONTEXT OF REGULAR CONSULTATIONS PROVIDED FOR WITH ALL MEMBERS IN THE REFORMED SYSTEM.

5. IF IN SUBSEQUENT PERIODS BALANCE OF PAYMENTS DEFICITS EMERGED FOR AN "INVESTMENT FUND" COUNTRY, FOR EITHER SHORT-TERM OR LONGER-TERM REASONS, THERE WOULD BE NO OBJECTION TO THEIR TRANSFERRING

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NEEDED AMOUNTS FROM THEIR "INVESTMENT FUND" TO THEIR REGULAR "RESERVES," SO THAT THESE FUNDS COULD BE USED TO FINANCE PAYMENTS DEFICITS.

THE PROVISIONS OF THE U.S. PROPOSALS CONCERNING CONVERTIBILITY WOULD NOT RAISE SPECIAL PROBLEMS OR NEED TO BE ALTERED IN RELATION TO OIL-PRODUCING COUNTRIES.

THE IDEAS IN THIS PAPER ARE INTENDED TO FACILITATE THE INITIATION AND MANAGEMENT OF "INVESTMENT FUNDS" IN A MANNER THAT WILL MEET THE REASONABLE INTERESTS AND NEEDS OF ALL PARTIES CONCERNED. AT BOTTOM, SUCH COOPERATIVE AND BALANCED

ARRANGEMENTS MUST MEET THE LEGITIMATE INTERESTS OF ALL CONCERNED TO BE PRACTICAL AND SUCCESSFUL. END QUOTE ROGERS

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